



BUDGET MONITORING REPORT

For the period from January to June 2012

Economic Performance

Revenues and expenditures are reported for the General Fund, Capital Investment Program Fund, Development Services Fund and the Utilities Funds.

The purpose of the report is to show how close the year-end projections are to mid-biennium forecast 2012 and discuss reasons for variance and convey the local as well as national economic outlook.

Overall, the international and U.S. economies are struggling to recover and are facing downside risk. While the local economy is outpacing the national economy in terms of employment and personal income growth, a slow housing market and lack of new construction is constraining growth.

The City of Bellevue expects revenue to be at the 2011-2012 updated mid-Biennium forecast. Cost saving measures implemented in 2011 remain intact and are necessary to better align expenses with revenue projections.

U.S. Economy

The U.S. economy continues to recover slowly with lagging employment. In June, U.S. employment grew by only 80,000 jobs, making for the third consecutive month of employment growth below 100,000. The **U.S. unemployment rate** has been hovering around **8.2%** since March 2012 (*U.S. Bureau of Labor Statistics*).

The Blue Chip consensus forecast predicts **real GDP growth at 2.1% in 2012**, revised down from a forecast of 2.3% in May. The downward revision was due primarily to risks associated with the sovereign debt crisis in Europe and the “fiscal cliff” the nation is approaching at the end of 2012 (*State of Washington Economic and Revenue Update – July 11, 2012*).

The **European sovereign debt crisis** continues to threaten global markets with instability. The recession caused several highly lever-

Performance at a Glance

YTD

Pg 4	General Fund YE Estimated Revenue vs General Fund YE Estimated Expense	+
Pg 5	Tax Performance as Compared to Revised Forecast	+
Pg 6	General CIP Expenditures & Resources vs Adopted Budget	-
Pg 7	Development Services YE Estimated Expenditures vs YE Estimated Revenues	O
Pg 7	Utilities Expenditures & Resources vs Adopted Budget	+

Compared to seasonal trends:

- +** = Positive variance or negative variance < 1%.
- O** = Negative variance of 1-4%.
- = Negative variance of > 4%.

aged European countries to become undercapitalized, increasing their sovereign default risk.

The “**fiscal cliff**” refers to a set of major fiscal events which may occur at the end of 2012, including the expiration of tax-relief provisions (e.g., Bush-era tax cuts, payroll tax cuts) and automatic federal spending cuts of \$1 trillion (*WA Economic and Revenue Update*). A large contraction in federal spending could pose a very serious threat to the economic recovery, potentially leading the country back into recession. The Congressional Budget Office estimates that ending these tax-relief programs would have the dual effect of quickly reducing the federal deficit and reducing GDP growth in 2013 from 4.4% to just 0.5%; it is likely that Congress will postpone consideration of the programs until after the November election, continuing the uncertainty and slow growth that has impeded the national economy.

Regional Economy

Despite the slow U.S. recovery and the aforementioned downside risks, the economy in the State of Washington seems to be recovering. **Washington personal income growth in early 2012 was among the strongest in the nation at 5.7%** compared to U.S. average of 3.4% (*WA Economic and Revenue Update*).

The forecast for the Puget Sound region calls for a **2.8% increase in employment**, a **5.4% rise in nominal personal income** and a **7.6% unemployment rate in 2012**. However, these forecasts presume no major shocks to the economy which may be unrealistic given the slowing growth in China, uncertainty in Europe and the “fiscal cliff” (*Puget Sound Economic Forecaster – June 2012*).

Bellevue Economy

Business activity in Bellevue has been increasing, with many leading economic indicators showing positive signs. Like the rest of the region, Bellevue is expected to outpace the national recovery. Bellevue has had **new businesses** opening and **increases in condominium sales** in several high rise buildings that have been largely unoccupied since 2008.

Central Business District office vacancy rate continues to drop, down to 13.4% from 13.8%, though it has slowed some from 2011 activity. Year-to-date office space absorption is on par with 2011 experience. Bellevue's **rent has continued to rise**. (*Cushman Wakefield Alliance Research Publication*).

Puget Sound Annual Percent Change		
	<u>2011 Actual</u>	<u>2012 Projected</u>
Employment	1.8%	2.8%
Personal Income	5.5%	5.4%
Housing Permits	11.1%	30.9%
Average Home Price	(9.6)%	(3.0)%
Taxable Retail Sales	(0.3)%	2.4%
* Source: Puget Sound Economic Forecaster—June 2012		



Art on display at Bellevue City Hall

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Housing

The real estate market appears to have finally bottomed out for the Pacific region in March 2012 (*Federal Housing Finance Agency – June 21, 2012*).

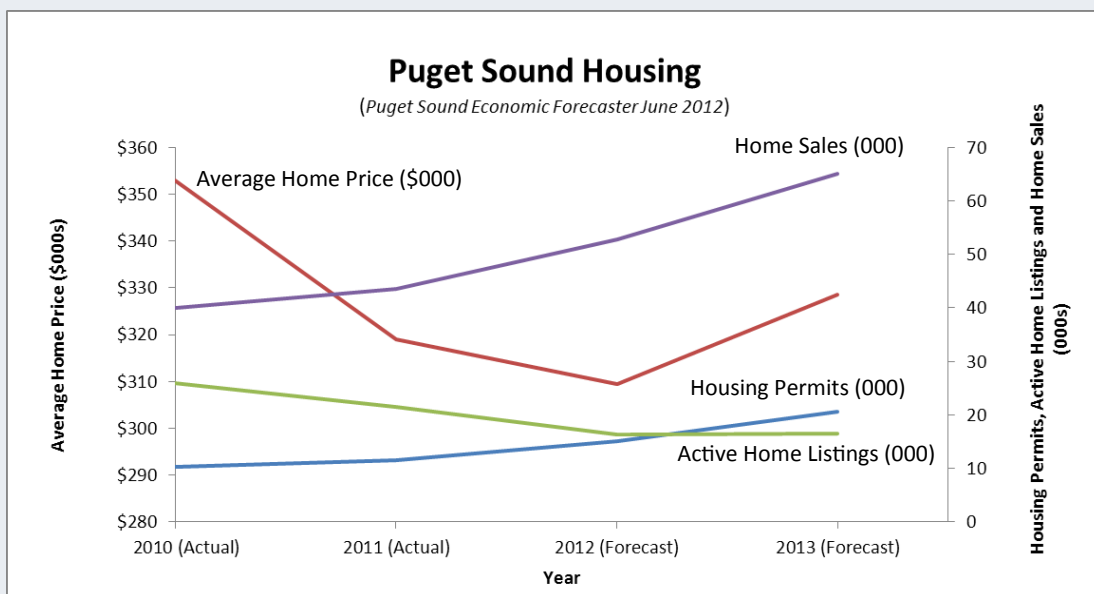
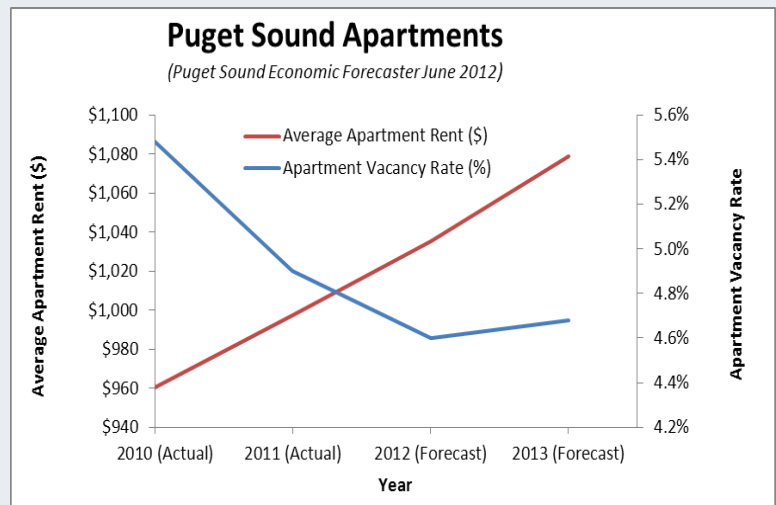
During previous recessions, property values were left largely untouched, providing a foundation for expedited recovery. However, one of the defining characteristics of the recent recession is the prolonged impact on property values and a decline in housing. The recovery of the housing sector will play a very important role in boosting the local economy. Doubts about the economy and home seekers' difficulty securing financing have thwarted the recovery of the housing sector. However, currently, **homes in the Puget Sound region are relatively affordable**: average home prices have declined 30% since 2007 and mortgage rates are at a record-low (*PSEF*).

Declining property values and volatility in the housing market have driven many Puget Sound residents into apartments. The first quarter of 2012 marked the **historically low apartment vacancy rate** of 4.6% while the **average rent climbed to an all-time high of \$1,017** (*PSEF*).

As rents rise and apartment vacancies become increasingly difficult to find, people will choose to purchase a residence, causing a greater demand for homes and a reduction in the current housing inventory.

The Puget Sound Housing chart below shows increasing home prices due to the decline in availability of single-family homes on the market. This situation provides incentive for construction activity, as seen in the slow rebound of housing permits, boosting the overall economy.

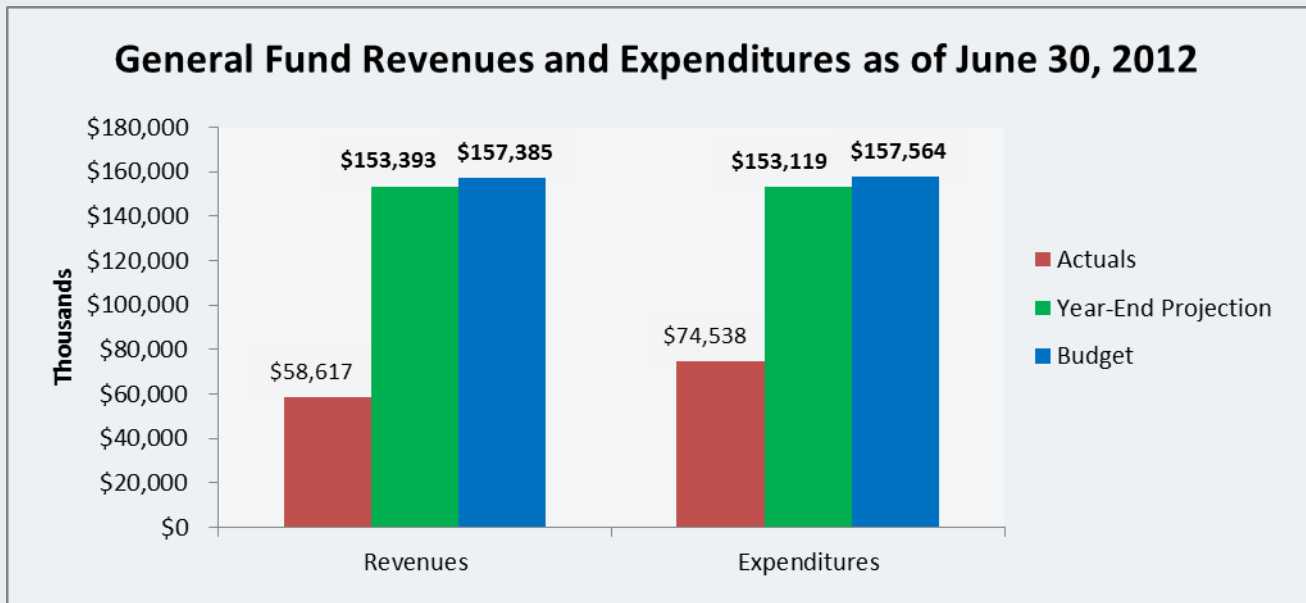
Also, the end of May marked the **groundbreaking of one of the two Soma Towers**, a high rise building located downtown at NE 2nd and 106th Avenue. This is the first large scale construction project in Bellevue since the 2008 real estate crash (*Seattle Times—May 2012*) and represents a bright spot on the horizon for increased economic activity in Bellevue.



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GENERAL FUND PERFORMANCE



NOTE: The above graph illustrates the difference between year-to-date revenue collections and expenditures through June, current year-end estimates, and adopted budget. Due to the time lag between earning and receiving some major tax collections, year-to-date actuals are less than actual second quarter activities. Expenditures are based on actual activities performed during the second quarter.

The primary revenue sources for the general fund include property tax, sales tax, and business and occupation tax. Together, sales tax and business and occupation tax comprise about 38% of the General Fund revenue. Both of these revenue sources are highly dependent on the local economy.

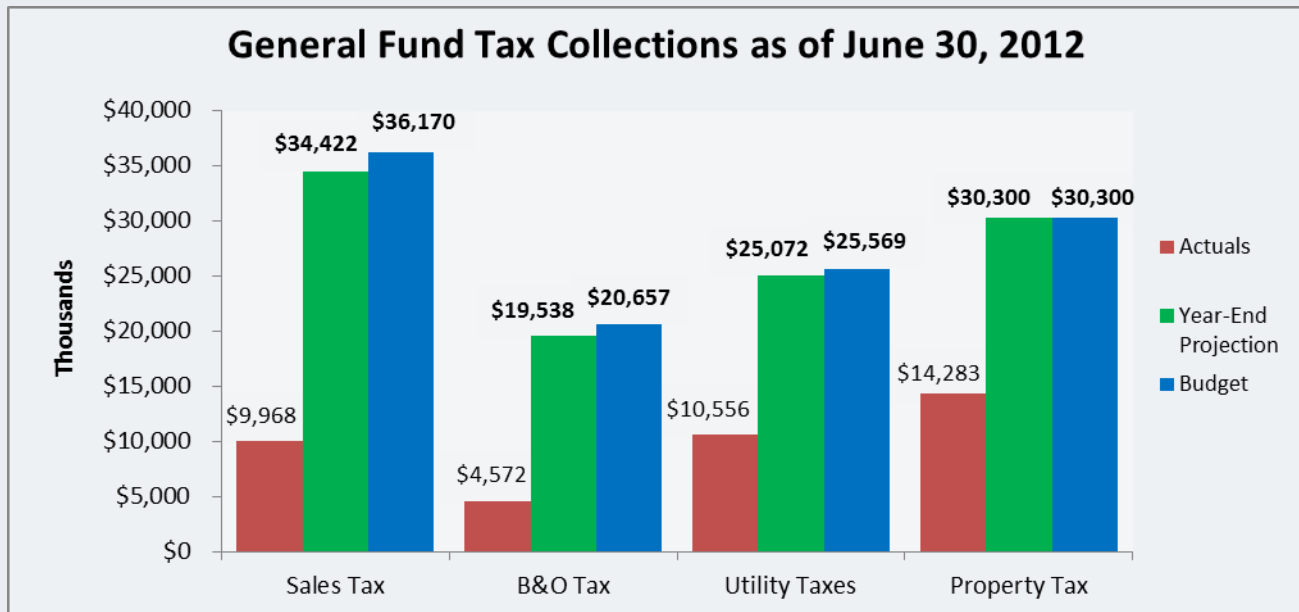
As has been reported previously, the Great Recession impacted the economically sensitive revenues, specifically business and occupation tax and sales tax. The chart above compares the budget for 2012 (adopted in December 2010) to the 2012 year-end estimate. The year-end estimates portray the effects of the Great Recession with reduced revenues.

Cost Containment

During the November 2011 mid-biennium update, the City of Bellevue enacted extensive cost containment measures and the City Council authorized the collection of additional revenue. The management actions taken in 2011 have brought expenditures below estimated revenues.

Revenue and expenditure projections above reflect the most current information. These projections are different than the projections reported to Council on July 30th. The information reported on July 30th aligned with 1st quarter projections (with a few known adjustments) as the 2nd quarter had not yet closed or been reconciled. The Budget Office is closely watching spending and revenue collections as the economy continues to recover.

GENERAL FUND PERFORMANCE



NOTE: The above graph illustrates the difference between year-to-date collections through June, current year-end estimates, and adopted budget. Due to the time lag between earning and receiving some major tax collections, year-to-date actuals are less than actual second quarter activities. Additionally, year-end projections are based on the limited information available to date. Projections, which are based on economic trends and projections as well as historical collections, will be updated as more information becomes available.

Tax Revenues

As has been reported previously, the Great Recession impacted the economically sensitive revenue, specifically business and occupation tax and sales tax. Consequently, during the mid-biennium update the forecast was revised downward although the adopted budget was not adjusted. The chart above compares the adopted budget for 2012 (adopted in December 2010) and the 2012 year-end estimate. The budget was revised during the mid-biennium update to reflect the impact of the Great Recession.

Sales Tax: Sales tax is collected two months in arrears. Therefore, as of this publication's date of June 30, the City has collected five months of sales tax. Sales tax is on track to meet updated mid-biennium projections of \$34.4M.

Business and Occupation Tax (B&O Tax): B&O tax collections to date appear low because of the accrual method and delay in processing, but are on track to exceed the mid-biennium revised forecast of \$19.5M.

Utility Taxes: Consistent with seasonal trends, utility tax collections

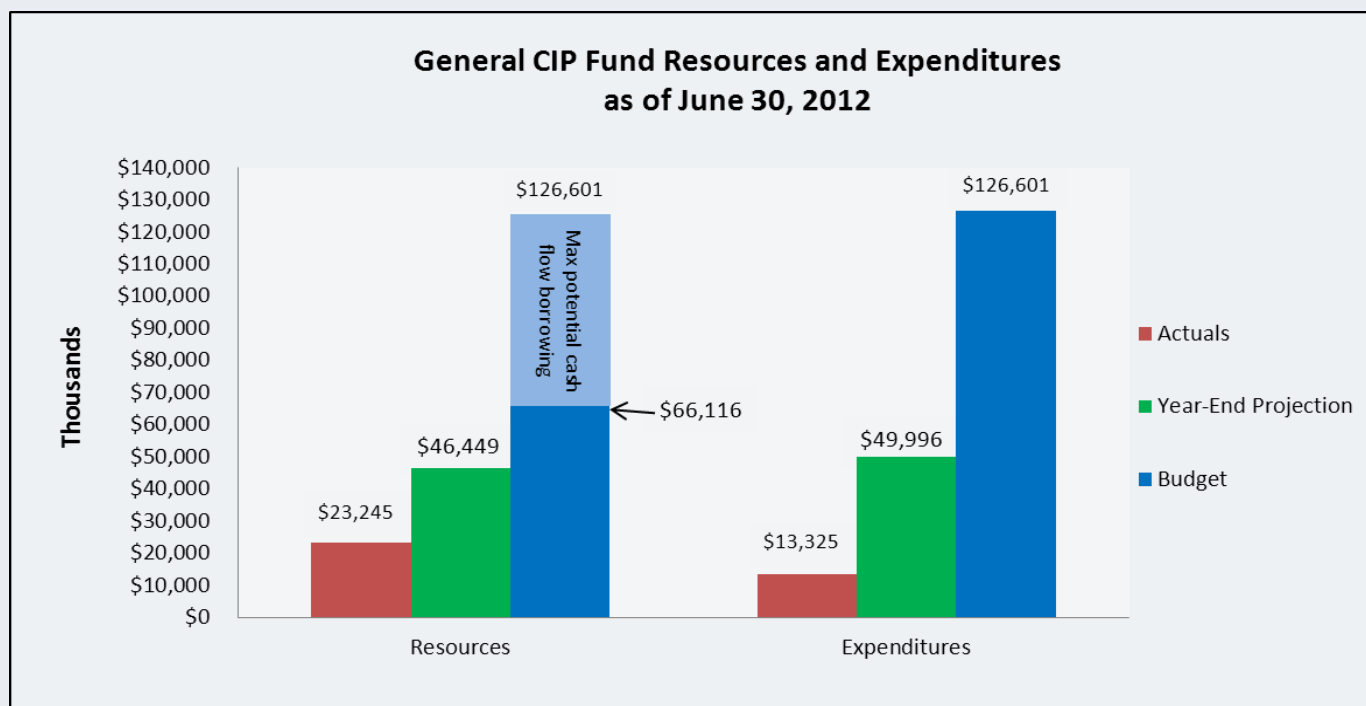
are expected to be slightly below budget primarily due to a shortfall in telephone and cellular tax. This shortfall is partially offset by over collections in gas and electric utility taxes. Overall, utility taxes are expected to be on target with updated year-end projections. Utility taxes are directly tied to utility rates—i.e. if Puget Sound Energy is approved for a rate increase, utility tax revenue would increase.

Property Tax. Property tax is determined based on the assessed value of properties within Bellevue. This figure is not as volatile as sales and B&O tax and is projected to be at adopted budget.

The Impact of the end of the Liquor Excise Tax

Along with the implementation of Initiative 1183 and the end of state-run liquor stores, the Washington State Legislature suspended the portion of excise taxes going to local governments until June 30, 2013. This represents a **loss in tax collections** for the City of Bellevue. In 2011, liquor excise taxes from the State of Washington amounted to over \$660,000 in revenues for the City of Bellevue. Losing the liquor excise tax in June of 2012 means a loss of about \$330,000 for 2012 and the full \$660,000 in subsequent years.

GENERAL CIP PERFORMANCE



NOTE: The above graph illustrates the difference between year-to-date resource collections and expenditures through June, current estimates, and adopted budget. Due to the time lag between earning and receiving some major tax collections, year-to-date actuals are less than actual second quarter activities. Expenditures are based on actual activities performed during the second quarter.

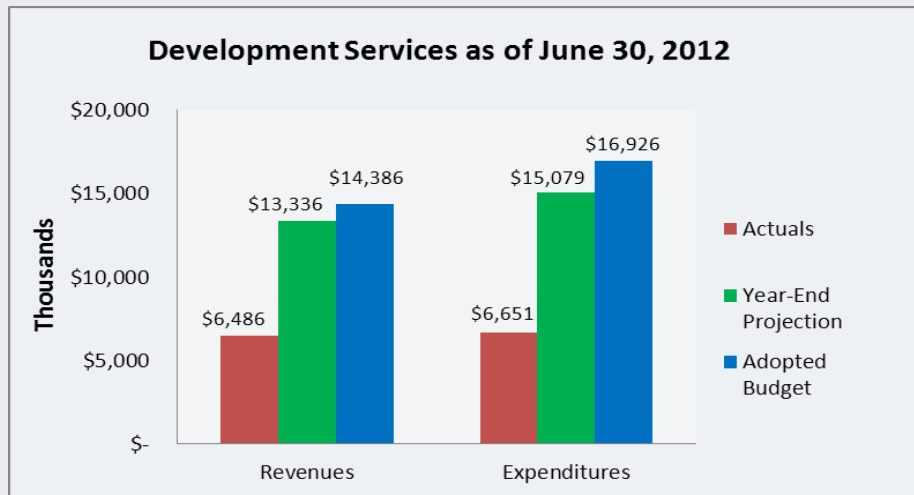
The City's economically sensitive revenues, specifically business and occupation tax and sales tax, have yet to return to pre-recession levels. The chart above compares year-end projections to the 2012 adopted budget (adopted in December 2010), portraying the impact of the Great Recession on City revenues. This analysis incorporates the timing of project expenditures and project specific revenues, such as grants and intergovernmental contributions, which are generally provided on a reimbursement basis. With the timing of major roadway projects such as NE 4th and 120th Avenue NE (Stage 1) pushed out over the next couple of years, grant revenues supporting the project will not be received until those costs are incurred.

For 2012, expenditures are currently projected to be approximately \$3.5 million greater than resources (comparing the green bars in the graph above). The City's policy to use temporary cash flow borrowing to bridge the gap between resources and

expenditures will effectively allow projects to move forward toward completion. Some major projects currently underway include the rebuild of Fire Station 5, fire station HVAC upgrades, and surface street overlays. In addition, neighborhood enhancement projects such as the Woodridge trail extension, Crossroads Community Garden, Larsen Lake Blueberry Farm enhancement, and Lewis Creek Park picnic area have been completed.

The City currently has a \$30.0 million line of credit (LOC) with \$15.0 million drawn to date, therefore the projected imbalance in 2012 can be managed by the existing capacity in the current LOC. **Staff is closely watching spending and revenue collections as the economy continues to recover to determine the impacts on the CIP** and any subsequent cash flow needs in 2012. The LOC is scheduled to come due in November 2013 and is included in the proposed 2013-2014 budget.

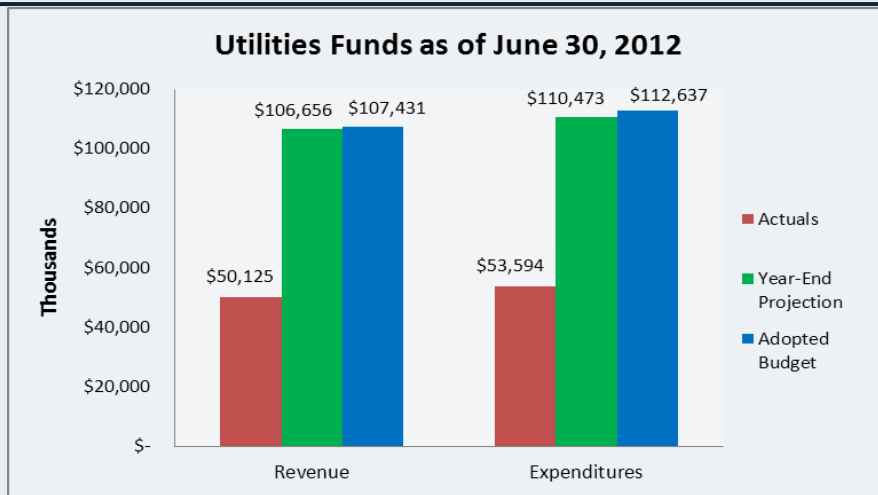
DEVELOPMENT SERVICES PERFORMANCE



Development Services **revenue collections are below anticipated levels in the second quarter.** Development permit applications continue to come in, however the size and scope are smaller which has resulted in decreased revenues. Development activity has grown slightly in 2012 over 2011 levels and is projected to have additional growth by year-end. Development Services year-end

expenditure projection reflects expenditure control measures implemented in prior years. Savings will be realized through position vacancies and reduction in contracted services. By policy, reserves are held to address revenue shortfalls in downward cycles.

UTILITIES PERFORMANCE



Expenditures are projected to exceed revenues by \$3.8 million in 2012, of which \$2.7 million are expenditures from 2011 projects that carried-forward into the current year. These expenses are fully funded through previous rate collections. The remaining \$1.1 million will be addressed through temporary use of reserves and the implementation of cost containments measures over the forecast period. Utility revenues are expected to be \$0.8 million below

budget due to low water sales and low interest earnings. Water wholesale costs will be about \$1.1 million below budget due to changes in Cascade Water Alliance's cost projections and revisions to ratemaking methodology. Expenditures are expected to show additional savings of about \$1.0 million largely due to reduced capital expenditures in the Water fund.

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